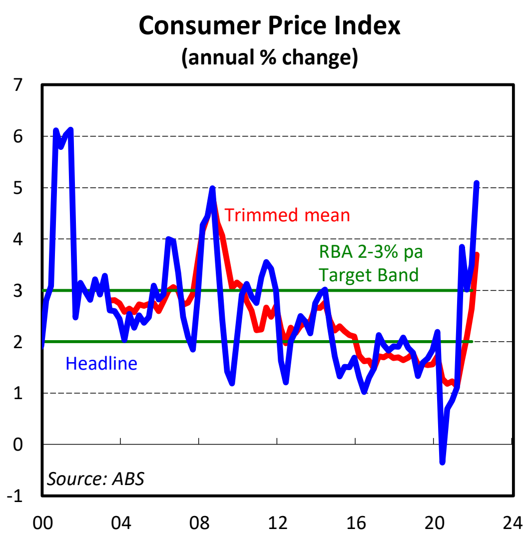
Data snapshot

Wednesday, 27 April 2022

# Consumer Price Index

## Odds for Rate Hike Next Week Shorten

- **Consumer prices pressures are mounting at an astonishing rate, blowing the Reserve Bank's forecasts and consensus forecasts out of the water. And the pressures are broad-based.**
- **In the March quarter, the headline consumer price (CPI) index rose a whopping 2.1% in quarterly terms to be 5.1% higher in annual terms. This is the hottest reading in quarterly and annual terms since the GST was introduced in the early 2000s.**
- **And trimmed mean inflation, which strips out more volatile price changes, will be making the Reserve Bank (RBA) sweat. This rose 1.4% in the quarter – the biggest quarterly jump since the December quarter in 1990 – to be 3.7% higher in annual terms.**
- **Price pressures have grown with the recovery in demand as we learn to live with Covid, plus supply disruptions, and labour and material shortages. The Ukraine war contributed to higher prices at the petrol pump while flooding in NSW and Queensland pushed up food prices.**
- **Annual non-discretionary inflation hit a huge 6.6%, more than double discretionary inflation, consistent with consumers reducing discretionary spending in lockdowns.**
- **Ahead of today's data, our central expectation has been for the RBA to kick off hiking from June. Earlier in April, the central bank stated there would be important information "over the coming months" on inflation and labour costs, laying the groundwork for a move in June.**
- **But with inflation running materially hotter than expected, the odds of a rate hike at next week's meeting have shortened. Indeed, market pricing for the first hike was brought forward to May following today's print.**




### Headline and Underlying Inflation

Prices pressures are mounting at an astonishing rate, blowing the RBA's forecasts and consensus forecasts out of the water.

The numbers were strong across the board. The headline consumer price index rose a whopping 2.1% in quarterly terms to be 5.1% higher in annual terms. This marks the strongest reading in both quarterly and annual terms since the GST was introduced in the early 2000s.

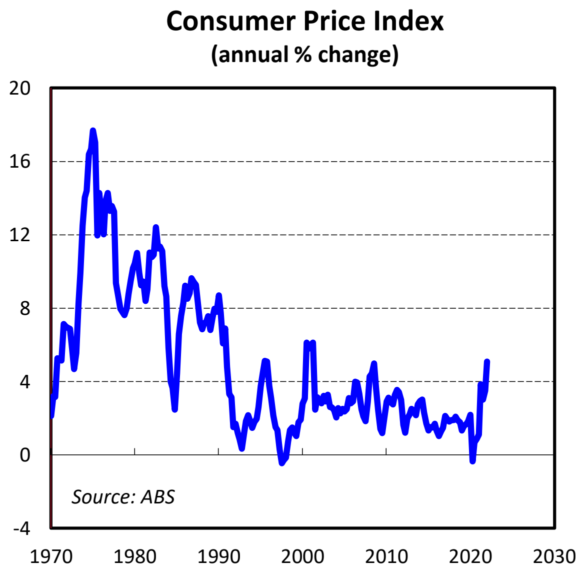
And trimmed mean inflation – which strips out more volatile price movements – will be making the RBA sweat. Trimmed mean inflation rose 1.4% in the quarter – the biggest quarterly jump since the December quarter in 1990 – to be 3.7% higher in annual terms. This indicates that the price pressures are broad-based.

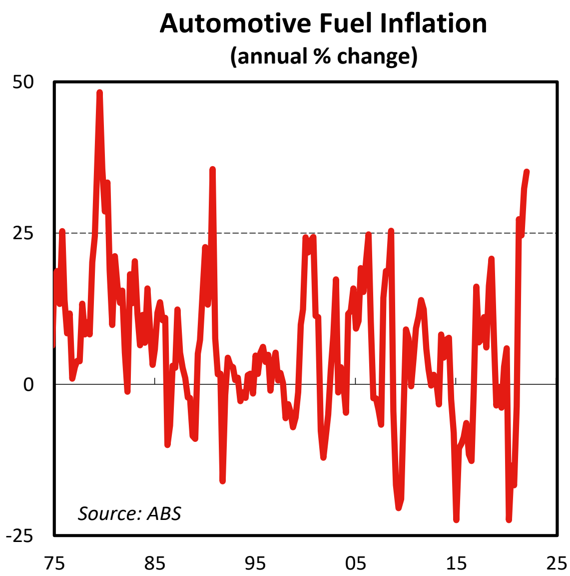
Trimmed mean inflation rose 1.0% in the December quarter, meaning that six-month annualised inflation is running at 4.8%. This measure last reached 4.8% in the September quarter of 2008.

Today's numbers are well above the RBA's 2-3% target band and appear significantly stronger than the central bank's forecasts. In their latest projections from February, the RBA expected annual trimmed mean inflation and headline inflation to reach 3.25% and 3.75%, respectively in the June quarter. And clearly, price pressures are already running hotter than this.

Ahead of today's release, our central expectation was for the RBA to kick off hiking from June. Earlier in April, the central bank stated there would be important information "over the coming months" on inflation and labour costs. This language laid the groundwork for liftoff in June but was predicated on the outlook evolving as expected.

However, inflation is running materially hotter than expected. In turn, it is possible the RBA board could decide they cannot afford to wait until June. This means we could see a rate hike at next week's meeting. Indeed, market pricing for the first rate hike was brought forward to May following today's print.




### Groups Analysis

Prices increased in ten out of eleven CPI groups and deflated modestly in one group.

The key drivers of the increase were transportation, which includes automotive fuels, education and housing.

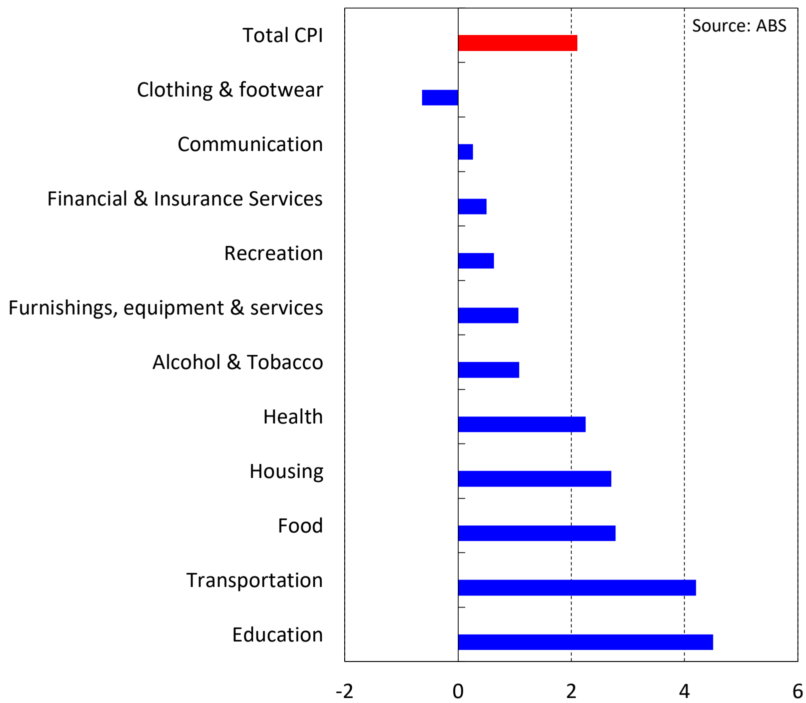
The Russian invasion of Ukraine and related spike in commodity prices, most notably in the price of crude oil, contributed to a 4.2% surge in transportation costs in the March quarter – a 31-year high. The rise in transportation costs was underpinned by an 11.0% jump in the price of automotive fuel, which is directly attributable to the surge in the price of crude oil. In annual terms, automotive fuels jumped 35.1%, the fastest annual pace since Iraq's invasion of Kuwait in 1990. The Federal Government's 50% cut to the fuel excise which was announced in the Federal Budget was not factored into the survey, as the change only came into effect on 30 March. As a result, fuel prices will be lower than otherwise in the June quarter.

Further increases in the price of motor vehicles as a result of lingering supply chain issues coupled with solid domestic demand also contributed to the rise in transportation costs in the March quarter.

The cost of education rose 4.5% in the March quarter, to be 4.7% higher in annual terms. A 6.3% jump in tertiary education relating to the implementation of a new fee structure prompted the rise. Secondary education (3.0%) and preschool and primary education (4.5%) also increased in the March quarter, alongside the commencement of the school year.

The cost of housing continued to accelerate in the March quarter rising 2.7% to an annual pace of 6.7%, the fastest since September 2008. The increase was largely attributable to a 5.7% quarterly increase in the cost of new dwellings purchased by owner-occupiers, which has been boosted by swelling construction costs and the unwinding of the government's Homebuilder scheme. Strong housing demand has meant that higher costs resulting from input and labour shortages are increasingly being passed onto consumers. Increases in the cost of rent and other housing related costs also contributed to the rise in prices, although were relatively more subdued.

**Price Changes of Selected CPI Categories**
**(Mar 2022, quarterly % Change)**




The price of food increased for a sixth consecutive quarter, jumping 2.8%, the fastest quarterly rise since the March quarter of 2011. Food prices increased across all sub-categories, led by fruit & vegetables (5.8%) and meat and seafoods (4.8%). Increases in the price of fresh food items were largely due to COVID-19 related supply chain disruption and increasing fertiliser and transport costs. Flooding in production areas of NSW and Queensland also contributed to the rising price of fresh food. The cost of meals out & takeaway foods increased 0.7% in the quarter, despite state government voucher initiatives such as 'Dine & Discover' which offset part of the rise.

Alcohol & tobacco and furnishings, household equipment & services each rose 1.1% in the quarter, to be up 1.8% and 4.9%, respectively in annual terms. An increase in alcohol prices following seasonal specials and a lift in the tobacco and beer and spirit excises were responsible for the rise in alcohol and tobacco prices. Among furnishings, household equipment & services, a 3.4% decline in furniture prices was more than offset by the remaining sub-components, including a 6.7% rise in non-durable household products such as toilet paper and paper towel. The cost of childcare was flat in the quarter, as increased fees were offset by additional subsidies which came into effect over the quarter.

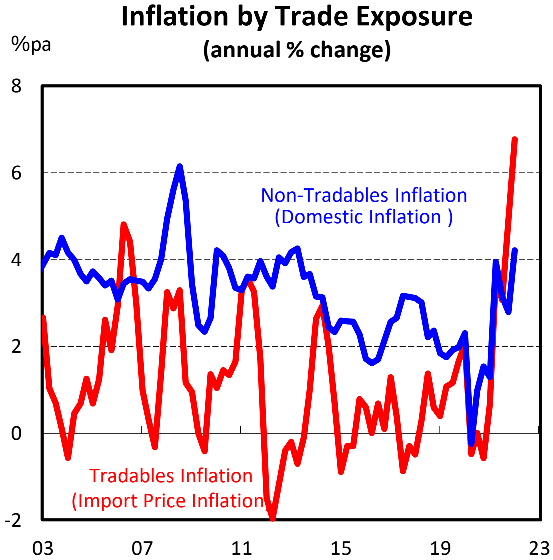
A strong rise in the cost of pharmaceutical products and a cyclical reduction in the proportion of people who qualify for subsidies under the pharmaceuticals benefits scheme (PBS) underpinned a 2.3% increase in health costs. Recreation (0.6%), financial & insurance services (0.5%) and communication (0.3%) groups experienced more modest price increases over the quarter.

Clothing and footwear was the only group to record a decline in prices over the quarter, easing 0.6% as excess stock was discounted heavily. Prices for clothing and footwear are 1.5% lower in annual terms.

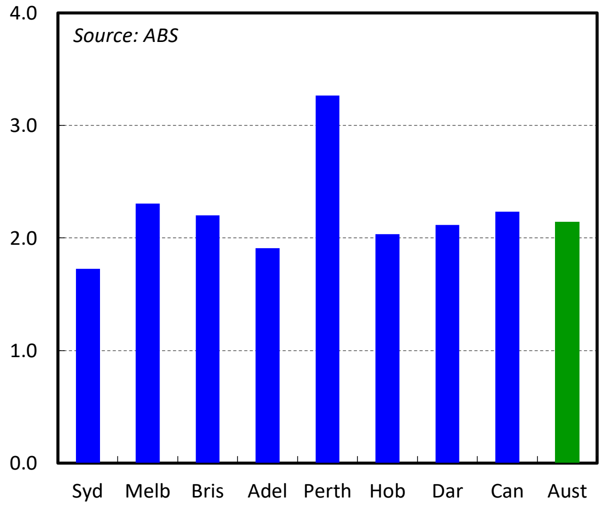
### Discretionary and Non-Discretionary Inflation

Non-discretionary inflation was running at a whopping 6.6% over the year to the March quarter, more than double discretionary inflation at 2.7%. Non-discretionary inflation captures goods and services that households are less likely to reduce their consumption of, such as food, fuel, housing and health costs. This is consistent with households reducing discretionary consumption alongside lockdowns.

**Inflation by Trade Exposure**
**(annual % change)**




**Inflation by Capital City**
**(quarter % Change, Q1 2022)**




### Tradables and Non-tradables Inflation

Tradable inflation spiked a record 2.8% in the March quarter, while non-tradable inflation increased 1.8% over the same period. The tradable inflation series includes goods and services that are highly exposed to international trade, such as automotive fuel and most food items. The non-tradable series includes goods and services which are mostly influenced by domestic factors, such as housing and education.

As expected, global inflationary pressures and the geopolitical conflict which erupted over the March quarter, has translated into a strong spike in tradable inflation. However, non-tradable inflation is also on the move, rising at its fastest quarterly pace since the introduction of GST in the September quarter of 2000.

The spike in tradable inflation was underpinned by a sharp rise in tradable goods in the quarter (2.9%), reflecting higher automotive fuel costs. This was partially offset by an 8.4% decline in tradable services, owing to cheaper international travel. In annual terms, tradable inflation jumped to a record high at 6.8%, eclipsing the previous record of 5.3% set in the June quarter 2001.

Meanwhile, the rise in the non-tradable inflation recorded in the March quarter was broad-based across both goods (2.9%) and services (1.2%). This was underscored by large price increases for the purchase of new dwellings and for tertiary education. Non-tradable inflation increased at an annual rate of 4.2%, the fastest pace in 8½ years.

## Inflation by capital cities

Inflation accelerated across all capital cities in the March quarter, save for Hobart. Perth (3.3%) led the way, followed by Melbourne (2.3%). Both cities recorded the fastest quarterly pace of inflation in over 21 years, since the September quarter 2000. Brisbane (2.2%), Canberra (2.2%), Darwin (2.1%) and Hobart (2.0%) all recorded quarterly inflation above two per cent, while inflation was slightly softer in Adelaide (1.9%) and Sydney (1.7%).

The surge in prices in Perth over the March quarter was underpinned by a more pronounced increase in housing costs, while sharp rises in the prices of automotive fuels, housing costs and food items were the main contributors to inflation across the capital cities.

In annual terms, inflation ranged from 7.6% in Perth, to 4.4% in Sydney. Inflation reached its fastest annual pace 13½ years in Sydney, Melbourne and Adelaide, while annual inflation hit a more than 20-year high in Brisbane and Canberra. At 7.6%, the annual pace of inflation in Perth is the highest since June 1990.

## Outlook

Today's data have shortened the odds of the RBA lifting the cash rate next week. Our central expectation is the central bank will kick off hikes from June, but an earlier move cannot be ruled out. Indeed, interest-rate markets are now fully priced for a 15 basis point rate hike in May, brought forward from June. The RBA previously suggested they would like to see the next wages print in on May 18 but it could be possible the board decides they cannot afford to wait that long.

We expect inflation will remain elevated over the remainder of the year before pressures begin to ease in 2023.

And the labour market is set to tighten even further. We expect the unemployment rate will fall below 3.5% later this year. There are widespread reports of labour shortages. Inevitably, this will feed through to higher wages and broader price pressures.

On this backdrop, an RBA rate hike is just around the corner.

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